Overview of Islamic Finance in Pakistan

- Started in 1977-78, which included the elimination of interest from the operation of specialized institution and commercial banks.
- Financial and corporate system was amended on June 26, 1980 to permit issuance of new interest-free instrument of corporate financing named ***Participation Term Certificate*** (PTC).
- In the same time Ordinance was promulgated to allow the establishment of ***Mudaraba*** companies and floatation of Mudaraba certificates for rising risk based capital.
- July 1, 1985, all commercial banks in Pak Rupee was made interest free which was ***mark-up*** technique with or without buy-back agreement. This was however declared un-Islamic by the Federal Shariat Court (FSC) in Nov 1991.

Overview of Islamic Finance in Pakistan

September 06

- ***Commission for Transformation of Financial System*** (CTFS) was constituted in January 2000 in the State Bank of Pakistan.
  - It introduced Shariah compliant modes of financing which included creating legal infrastructures conductive for working of Islamic financial system, launching a massive education and training program for bankers and their clients and an effective through media for the general public to create awareness about the Islamic financial system.
  - It also dealt with major products of banks and financial institution , both for assets and liabilities side

Overview of Islamic Finance in Pakistan

September 06

- In September 2001 it was decided by Government that the shift to interest free economy would be made in a gradual and phased manner and without causing any disruptions and was also agreed that state bank Pakistan would consider for:
  - Setting up subsidiaries by the commercial banks for the purpose of conducting Shariah compliant transactions
  - Specifying branches by the commercial banks exclusively dealing in Islamic products, and
  - Setting up new full-fledged commercial banks to carry out exclusively banking business based on proposed Islamic products.
- In January, 2002 State Bank of Pakistan gave first Islamic Banking License to ***Meezan Bank Ltd***.

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Present State of Pakistan Islamic Banking

September 06

- The progress of Islamic Banking in Pakistan has been commendable during the last two years
- There is huge appetite for Islamic financial services. The growth, is however, constrained by the lack of infrastructure support & dearth of professional Islamic Bankers

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Present State of Pakistan Islamic Banking

September 06

- Currently, there are
  - 6 licensed full fledged (4 operational) Islamic Banks with 40 branches
  - 10 conventional banks with standalone Islamic Banking Branches with the total branch network of 35 branches operating in thirteen cities of all the four provinces in the country (as of 31 March 2005)
  - Applications for a few more banks are under consideration
- The central bank is pursuing a three-pronged strategy to promote Islamic Banking in Pakistan
  - establishing full-fledged Islamic banks in the private sector;
  - setting up of subsidiaries by the existing commercial banks; and
  - allowing stand-alone branches for Islamic banking by the existing commercial banks

International Islamic Financial Market

- Currently, Islamic Banking Sector operates under the existing laws & regulations for conventional banks
- The State Bank of Pakistan (SBP) established the Islamic Banking Department on 15 September 2003.
- The Department was given the task of promoting & developing the Shariah Compliant Islamic Banking as a parallel & compatible banking system in the country

Regulation of Islamic Capital & Money Market September 06

- Currently, the Islamic Banking Department (IBD) consists of the following three divisions
  - Policy Division
  - Shariah Compliance Division
  - Business Support Division
- To regulate & supervise the Islamic Banking Sector SBP is working on the areas of Risk Management, Corporate Governance, Prudential Regulations, Accounting & Shariah Standards etc.
- A Shariah Board is also in place at the State Bank of Pakistan, having experts to guide the Islamic banking industry

Key Figures of Islamic Instruments

September 06

- Sukuk
  - Government of Pakistan Sovereign Sukuk – USD600 million 5year, Libor +220bps,
  - Water & Power Development Authority Sukuk USD 133.33 million -Domestic Issue
- Modaraba
  - There are 36 Madarabas as on 2nd August 2006.
  - Total assets of Modarabas - USD352.12 million & paid-up capital of USD123.43 million as on 30 June 2005
  - Net Profit Margins - 20.15%
- **DEPOSITS**
  - Till March 2006, Islamic Banking Deposit increased to USD 1.3billion which is 2.8 of the total deposit of the commercial banks
  - Share of Islamic banking in the overall banking system increased to 2.1pc from 2.0pc

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presents the
3rd Annual Asian
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Key Figures of Islamic Instruments

September 06

- Mutual Funds (30 June 2005)
  - Meezan Balanced Fund- total assets USD 24.3million
  - Meezan Mutual Fund – total assets USD 29 million
  - Meezan Islamic Fund – total assets USD 34.5 million
  - Pakistan International Element Islamic Fund – total assets USD 22 billion
- TFCs
  - Sitata Chemical Industries Ltd. - Musharakah based TFCs USD 6 million
  - Al-Zamin Leasing Modaraba I tranch- Musharakah based TFCs USD 5 million
  - Al-Zamin Leasing Modaraba II tranche - Musharakah based TFCs USD 5.42 million

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Key Figures of Islamic Instruments

September 06

Market Size in terms of Market Capitalization

Panel-A: Main Sample

	Market Capitalization USD billion			Market Capitalization as per cent of GDP		
	(2002)	(2003)	(2004)	(2002)	(2003)	(2004)
Bahrain	7.58 a			98.7 a	120 b	122.2c
Malaysia (KLSE)	122.9	168.6	190	130.0	171.8	
Pakistan (KSE)	9.7	16.26	24.7	13.5	19.7	26.0
Sudan	0.593	0.734	1.4	4.0	4.3	

a. Calculation based on data from BSE Annual Report on Mkt Cap and IFS data for exchange rate and GDP.
b. Calculation based on the value of Mkt Cap reported in BMA Annual Report 2003 and GDP for 2003 (at constant prices) reported in MBA Islamic Finance Review, Jan 2005 issue 8.
c. Calculation based on value of Market Capitalization as of Sep. 2004 reported in Bahrain Stock Exchange 3rd Quarter Highlights 2004 and GDP at current prices (local currency) 2004 reported by IMF World Economic Outlook Database.
Data for Pakistan (KSE) is from State Bank of Pakistan (SBP) Financial Markets Report (2004), Chapter-4. Conversion into USD is made using Average Exchange Rates for each year given in SBP Annual Report 2004.

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Key Figures of Islamic Instruments

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Panel-B: Size Comparison with some other OIC countries and World

Country	Market Capitalization				S&P/IFC Investable Index	
	Million USD		% of GDP		% change in price index	
	1990	2004	1990	2003	2003	2004
Bangladesh	321	3,317	1.1	3.1	15.4	104.3
Egypt	1,760	38,576	4.1	32.8	79.3	126.4
Indonesia	8,080	73,251	7.1	26.2	69.7	39.3
IR Iran	34,300	34,444	--	25.1	--	--
Jordan	2,000	18,383	49.7	111.2	65.4	55.0
Kazakhstan	--	2,425	--	8.2	--	--
Kyrgyz Rep.	--	31	--	1.6	--	--
Lebanon	--	2,321	--	7.9	0.9	53.5
Morocco	966	25,064	3.7	30.1	44.0	18.3
Oman	1,060	6,325	9.4	19.7	47.0	25.2
Palestine	--	6,292	--	182.1	--	--
Saudi Arabia	48,200	306,248	36.7	73.2	49.5	83.6
Tunisia	533	2,641	4.3	9.8	14.9	4.2
Turkey	19,100	98,299	12.7	28.4	113.2	32.9
UAE	--	--	--	11.4	--	--
WORLD	*9,403,525*	*32,436,350*	*48.0*	*89.7*		
LIC	*46,543*	*319,611*	*10.5*	*37.3*		
MIC	*328,522*	*2,534,088*	*19.4*	*44.5*		
HIC	*9,028,460*	*29,582,653*	*51.6*	*100.1*		

LIC: Low Income Countries; **MIC**: Middle Income Countries; **HIC**: High Income Countries
Source: Complied from *World Development Indicators* (2005) Table 5.4 Stock Markets. World Bank.

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International Islamic Financial Market

Key Figures of Islamic Instruments

Trading Volume and Market Liquidity

Panel-A: Main Sample

	Trading Volume (No. of shares in millions)			Trading Value (Value of Transactions)			Turnover Ratio (Percent)		
	2002	2003	2004	2002	2003	2004	2002	2003	2004
Bahrain	353.13	405.60	288.42*	80.905 mil BD	102.261 mil BD	363.01 mil USD	1.78	1.74	2.69
Malaysia	---	116,853.1**	122,680.4	---	195.373 bil RM**	243.862 bil RM	---	30.5	33.8
Pakistan (KSE)	41,627.20	76,380.08	51,413.60	805 bil Rs	2270 bil Rs	4925 bil Rs	135.3	238.7	346.5
Sudan	4,060.23	9,745.45	2,185.99	24.906 billion SD = USD95 mil	24.41 billion SD	44.772 billion SD	16.0	13.0	12.0

* End of Nov. 2004.
** 11 month period Feb-Dec 2003
Data Sources:
Data for Bahrain: Bahrain Monetary Agency, Annual Report, various years; Bahrain Stock Exchange, Annual Report, various years; BMA, Islamic Finance Review, various issues.
Data for Malaysia: Calculated from data from KLSE Website
Data for Pakistan: are from SBP, Financial Markets Report, Chapter 4, Capital Markets. It covers only KSE for Fiscal Year (i.e. July of a year to June next year); IMF Pakistan Financial Sector Assessment 2003.
Data for Sudan: from annual reports of Khartoum Stock Exchange.

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Key Figures of Islamic Instruments

Panel-B: Liquidity & Listing Comparison with some other OIC countries and World

Country	Market Liquidity		Turnover Ratio		Listed Domestic Companies	
	Value Traded as % of GDP		Value of Shares Traded as % of Market Capitalization		Number	
	1990	2003	1990	2004	1990	2004
Bangladesh	0.0	0.6	1.5	36.1	134	250
Egypt	0.3	4.0	--	17.3	573	792
Indonesia	3.5	7.1	75.8	43.3	125	331
IR Iran	--	3.9	30.4	21.7	97	370
Jordan	10.1	26.4	20.0	36.3	105	192
Kazakhstan	--	1.4	--	22.0	--	41
Kyrgyz Rep.	--	--	--	58.1	--	17
Lebanon	--	0.7	--	10.3	--	13
Morocco	0.2	1.6	--	9.1	71	52
Oman	0.9	2.6	12.3	31.5	55	96
Palestine	--	1.7	--	1.7	--	27
Saudi Arabia	1.7	74.1	--	204.1	59	73
Tunisia	0.2	0.7	3.3	9.2	13	44
Turkey	3.9	41.4	42.5	182.3	110	296
UAE	--	0.0	--	3.4	--	--
WORLD	*28.5*	*83.4*	*57.2*	*72.4*	*25,424*	*50,038*
LIC	*5.0*	*42.5*	*48.2*	*130.5*	*3,321*	*7,988*
MIC	*5.1*	*21.6*	--	*60.9*	*4,370*	*14,456*
HIC	*31.4*	*96.8*	*59.4*	*110.1*	*17,733*	*27,594*

LIC: Low Income Countries; **MIC**: Middle Income Countries; **HIC**: High Income Countries
Source: Complied from *World Development Indicators* (2005) Table 5.4 Stock Markets. World Bank.

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Future Prospects

- The Government of Pakistan intends to continue promoting Islamic Banking in the country while keeping in view its linkages with the global economy & existing commitments to local & foreign investors
- There is a great need to develop instruments for liquidity management by banks & monetary management by the SBP
- The pace of Islamization of the financial system will crucially depend on the development of Shariah compliant instruments to be used for government transactions
- There is need for innovative products i.e., development of financial instruments on the basis of Musharika, Mudaraba, Leasing, & Salam – related to wide spectrum of maturities, projects & issuing entities

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